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THE CONGRESSIONAL BUDGET OFFICE'S UPDATED BUDGET OUTLOOK

HEARING

BEFORE THE

COMMITTEE ON THE BUDGET UNITED STATES SENATE

ONE HUNDRED SIXTEENTH CONGRESS

SECOND SESSION

September 23, 2020

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WEDNESDAY, SEPTEMBER 23, 2020

THE CONGRESSIONAL BUDGET OFFICE'S UPDATED BUDGET OUTLOOK

WEDNESDAY, SEPTEMBER 23, 2020

U.S. SENATE,
COMMITTEE ON THE BUDGET,
Washington, D.C.

The Committee met, pursuant to notice, at 2:29 p.m., in Room SD–608, Dirksen Senate Office Building, and via Webex, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Crapo, Toomey, Braun, Scott, Kennedy, and Van Hollen.

Staff Present: Doug Dziak, Republican Staff Director; and Mike Jones, Minority Deputy Staff Director.

OPENING STATEMENT OF CHAIRMAN MICHAEL B. ENZI

Chairman ENZI. Good afternoon. I will call the Committee to order.

Today the Committee will hear testimony from the Congressional Budget Office Director, Phillip Swagel, on CBO's updated budget and economic projections. These projections account for the effects of the COVID–19 pandemic and legislation enacted in response to it and provide a window into the future of our financial state.

This is Dr. Swagel's first time testifying before the Budget Committee since becoming the tenth Director of the Congressional Budget Office. Unfortunately, the pandemic has delayed us from having him appear before this Committee. I would like to thank Dr. Swagel for being here today. I would also like to thank the CBO staff for working to provide Congress with informed estimates at a time of unprecedented uncertainty and unusual working conditions.

CBO's updated budget projections confirmed what we all knew: that the economic disruption caused by COVID–19 and the Federal Government's response have led to a surge in deficits and debt. CBO projects that by the end of the month we will have spent $3.3 trillion more than we took in during fiscal year 2020, more than triple the size of last year's deficit, and the largest deficit relative to the size of our economy since 1945.

Our debt-to-Gross Domestic Product (GDP) ratio will close out the year at 98 percent, nearly 20 percentage points higher than it was at the end of the last year. Next year it is expected to climb above 100 percent for the first time since the end of World War II.

These staggering updated figures reflect the magnitude of the crisis presented by COVID–19 and the unprecedented actions Congress and the President have taken. In response to the pandemic and the ensuing lockdowns, we came together on a bipartisan basis to enact the largest relief package in United States history. We worked to alleviate the financial devastation and it helped, but at great cost.

CBO estimates that the legislation enacted in response to the pandemic will cost roughly $2.8 trillion. Sometimes the amounts we are discussing are so great that we lose context. That $2.8 trillion is the equivalent of $8,400 for each and every adult and child in this country. Adult and child in this country, $8,400. By all accounts, the U.S. fiscal response to COVID–19 was one of the largest, if not the largest among advanced economies. It is an extraordinary response to an extraordinary challenge.

But we face another extraordinary challenge. As the CBO demonstrates, our national debt continues growing long after the current crisis abates. CBO projects that the size of our publicly held debt, which already amounts to more than $60,000 for every adult and child, will soon exceed the size of our economy. And by 2023, the debt-to-GDP ratio will be the highest it has been in our Nation's history.

It will only keep growing from there. By 2050, debt will reach 195 percent of GDP. Deficit spending and the national debt was unsustainable before the pandemic. We must address it before it becomes the next historic crisis or prohibits future policymakers from dealing with future emergencies.

COVID–19 and the Government response to it are not the root of the cause of our long-term budget problem. Nevertheless, that does not mean we should continue to spend with impunity. While additional measures to combat the virus and help struggling families and businesses may be necessary, we cannot use this crisis to justify multi-trillion-dollar wish lists that have little or nothing to do with the pandemic.

Wasting billions bailing out mismanaged pension plans or providing tax breaks to wealthy individuals in high-tax States will not help us find a vaccine or spur the economic recovery. More spending will squander our limited fiscal capacity and saddle our children and grandchildren with an even higher debt.

Make no mistake: Debt and deficits matter. CBO warns that our rising debt will leave future generations with higher interest rates, lower incomes, and a greater chance of a fiscal crisis, which will lead to more painful options while we try to address it. We cannot continue running trillion-dollar annual deficits forever. The longer we wait, the more severe the challenges, and challenges will be, and the fewer options we have.

I look forward to hearing from our witness today. There is no person representing the other side, so we can move on to our witness.

Our witness today, as I mentioned, is Dr. Phillip Swagel, the Director of the Congressional Budget Office. Dr. Swagel became the tenth Director of the CBO on June 3, 2019. Prior to his appointment, he was a professor at the University of Maryland School of Public Policy and a visiting scholar at the American Enterprise Institute and the Milken Institute. Dr. Swagel was Assistant Secretary for Economic Policy at the Treasury Department from 2006 to 2009, and he has also served as Chief of Staff and Senior Economist at the White House Council of Economic Advisers and as an economist at the Federal Reserve Board and the International Monetary Fund. That covers just about all the financial bases.

For the information of colleagues, Dr. Swagel will provide us with an opening statement followed by questions.

Dr. Swagel, please begin.

STATEMENT OF THE HONORABLE PHILLIP L. SWAGEL, PH.D., DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Mr. SWAGEL. Thank you. Chairman Enzi, Ranking Member Sanders, and members of the Committee, thank you for inviting me to testify about CBO's budget update and the long-term budget outlook.

I will focus in my remarks now on that long-term fiscal challenge, and the challenge is daunting. At the same time, the United States is not facing an immediate fiscal crisis. The current low interest rates indicate that the debt is manageable for now and that fiscal policy could be used to address national priorities if the Congress chose to do so.

In our projections, interest rates remain low for several years and as the economy recovers from the effects of the pandemic, in part because the Federal Reserve is working to keep interest rates low.

Let me make two main points about the long-term outlook. Federal debt is high and is projected to rise substantially, number one. And, number two, over the long term, actions are needed to address the Nation's fiscal challenges. So here are some of the numbers.

The Federal debt held by the public is projected to increase to 98 percent of GDP at the end of this year. It is up from 79 percent last year and up from only 35 percent in 2007 before the start of the previous recession. And the debt is projected to continue to rise, reaching 195 percent of GDP by 2050, and that far exceeds the previous high of 106 percent recorded just after World War II.

So what has happened this year in 2020? Well, the year began with a strong economy and a strong labor market, but also with a deficit that was projected at $1 trillion. It was high already by historical standards, and then, of course, Mr. Chairman, as you said, the pandemic changed the situation dramatically. So our projection of the deficit this year has increased to $3.3 trillion, mostly reflecting the budgetary effects of legislation enacted to address the pandemic and, of course, the resulting economic downturn.

Now, at 16 percent of GDP, the deficit relative to the size of the economy is the largest since 1945. Over the next 30 years, debt will continue to rise, and that is because Federal spending is set to grow from 21 percent of GDP last year to 31 percent of GDP in 2050, and with interest costs contributing the most to that growth in spending. And, again, even as we project interest rates to remain low for several years as the economy recovers from the pandemic, and those low interest rates hold down borrowing costs.

The challenge is that continued deficits drive up the cost of servicing the debt, and spending growth also reflects rising costs for health care programs and for Social Security spurred by both the aging of the population and by projected growth in health care costs.

Federal revenues increased from 16 percent of GDP last year—again, before the pandemic—to 19 percent in 2050. The challenge with the long-term fiscal policy is that the path over the coming decades is unsustainable, and the cost of financing these deficits and servicing the debt cannot consume an ever-growing proportion of the Nation's income.

The consequences of this high and rising debt will play out for the economy. Borrowing costs will eventually rise, reducing business investment, slowing economic growth. The larger interest payments will go to foreign holders of U.S. debt, and that subtracts from our national income. And then a fiscal crisis in which interest rates abruptly escalate or other disruptions occur become a greater risk. And higher rates of inflation and the chance of a loss of confidence in the dollar have a greater chance of occurring.

Now, there is no set tipping point at which a fiscal crisis becomes likely or imminent, nor is there an identifiable point at which interest costs as a percentage of GDP become unsustainable. The challenge is that as the debt grows, these risks become greater.

Now, the status of the Federal trust funds is one indication that action may be needed soon, so in our projections, the Highway Trust Fund is exhausted in 2021; Medicare's Hospital Insurance Trust Fund is exhausted in 2024; Social Security's Disability Trust Fund is exhausted in 2026; and the main fund of Social Security, the Old-Age and Survivors Fund, is exhausted in 2031. So action is close, not over the horizon, but the fiscal challenge is close by.

Again, the current low interest rates on Treasury securities indicate that the Nation is not facing an immediate fiscal crisis, but we face fiscal challenges over the long term that will require difficult adjustments after we have emerged from the challenges of the pandemic.

Let me conclude and just take a moment, Mr. Chairman, to thank you on behalf of everyone at CBO. Thank you and your staff for your support for CBO and for our mission to serve the Committee and the Congress.

Thank you very much.

[The prepared statement of Mr. Swagel follows:]

PREPARED STATEMENT OF MR. PHILLIP L. SWAGEL

Congressional Budget Office

Testimony

The 2020 Long-Term Budget Outlook

Phillip L. Swagel
Director

Before the
Committee on the Budget
United States Senate

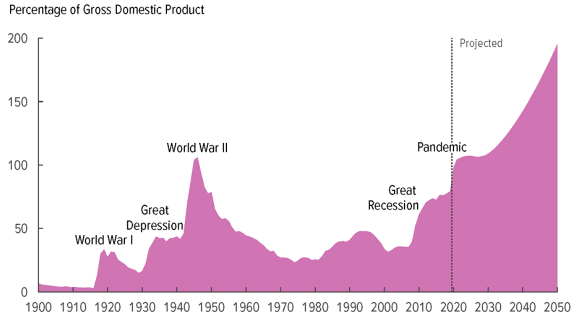
September 23, 2020

Chairman Enzi, Ranking Member Sanders, and Members of the Committee, thank you for inviting me to testify about the Congressional Budget Office's most recent long-term budget projections. Today, I will focus on the long-term fiscal challenges facing the nation that are the subject of the report that CBO released on Monday.

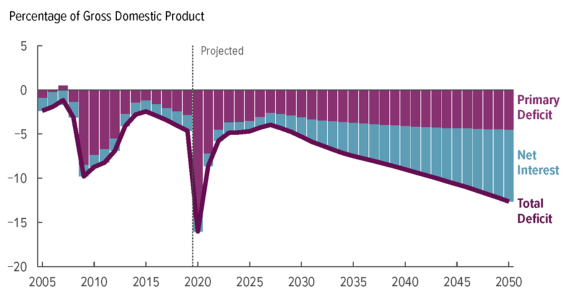
Each year, CBO issues a set of long-term budget projections—often referred to as the extended baseline projections—that provide estimates of what federal debt, deficits, spending, and revenues would be over the next 30 years if current laws generally remained unchanged. Relative to the size of the economy, federal debt is higher in this year's projections than it was in last year's projections. The economic disruption caused by the 2020 coronavirus pandemic and the federal government's response to it contribute significantly to that difference.

Debt and Deficits

Federal debt held by the public is projected to equal 195 percent of gross domestic product (GDP) in 2050, and the deficit is projected to equal 13 percent of GDP.

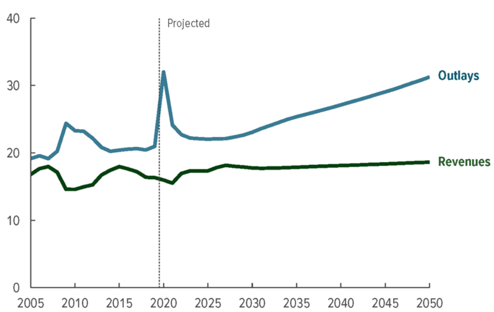


In CBO's projections, federal debt held by the public surpasses its historical high of 106 percent of GDP in 2023 and continues to climb in most years thereafter. In 2050, debt as a percentage of GDP is nearly 2.5 times what it was at the end of last year.



Deficits grow from an average of 4.8 percent of GDP from 2010 to 2019 to an average of 10.9 percent from 2041 to 2050, driving up debt. Net spending for interest rises rapidly and accounts for much of the growth in total deficits in the last two decades of the projection period.

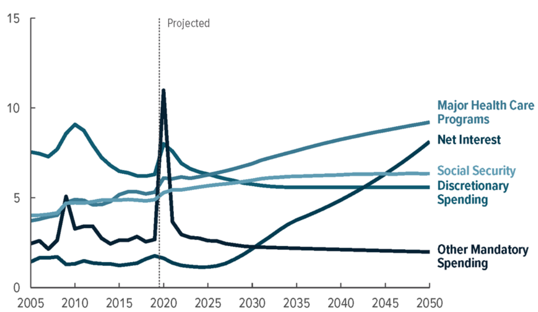
Debt and Deficits (Continued)



In CBO's projections, growth in outlays outpaces growth in revenues, resulting in larger budget deficits over the long run.

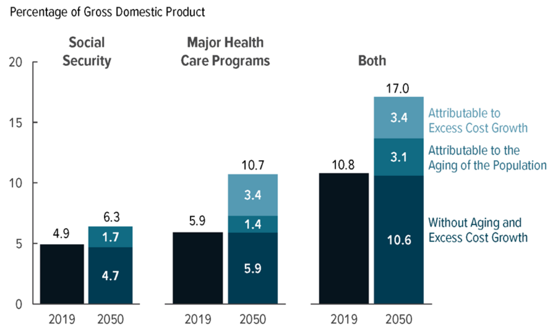
Spending

Federal spending grows from an average of 21.3 percent of GDP from 2010 to 2019 to an average of 29.3 percent from 2041 to 2050.



Net spending for interest, measured as a share of GDP, nearly quadruples over the last two decades of the projection period. In addition, after the effects of increased spending associated with the pandemic dissipate, spending as a share of GDP increases for the major health care programs and Social Security.

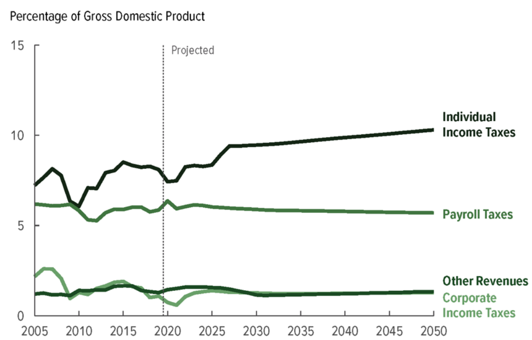
Spending (Continued)



Much of the growth in combined spending for Social Security and the major health care programs results from the aging of the population. Growth in spending for the major health care programs is also driven by excess cost growth—the extent to which the growth rate of health care costs per person (adjusted for demographic changes) exceeds the growth rate of potential GDP (the economy's maximum sustainable output) per person.

Revenues

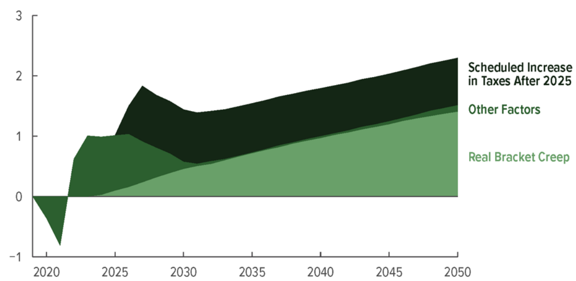
In CBO's projections, federal revenues increase from an average of 16.4 percent of GDP from 2010 to 2019 to an average of 18.4 percent from 2041 to 2050.



Increases in receipts from individual income taxes account for most of the rise in total revenues. Those receipts increase in 2025 because of the expiration of nearly all provisions of the 2017 tax act that affect individual income taxes.

Revenues (Continued)

Percentage of Gross Domestic Product

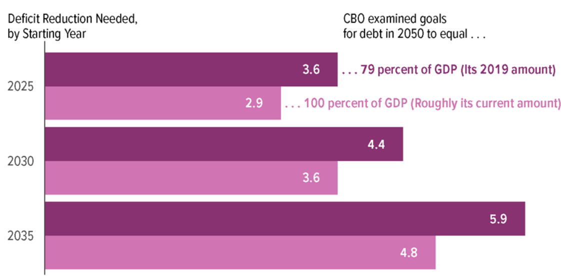


Over the long term, the largest source of growth in tax revenues is real bracket creep—the process in which, as income rises faster than inflation, a larger proportion of income becomes subject to higher tax rates.

Policy Changes Needed to Meet Various Targets for Debt

The reduction in the annual primary deficit (which excludes net spending for interest) needed to make federal debt held by the public in 2050 equal a certain goal would be smaller the sooner the policy changes were implemented.

Percentage of Gross Domestic Product



Even if policymakers took action soon, significant cuts to primary deficits would be necessary for debt to equal 100 percent of GDP in 2050.

The 2020 Long-Term Budget Outlook is one of a series of reports on the state of the budget and the economy that the Congressional Budget Office issues each year. This testimony summarizes that report. In keeping with CBO's mandate to provide objective, impartial analysis, neither that report nor this testimony makes any recommendations.

The full report and supplemental data files, which were prepared by many people at CBO, are available on the agency's website at www.cbo.gov/publication/56516. This testimony is available at www.cbo.gov/publication/56607.

Phillip L. Swagel
Director

CBO

Chairman ENZI. Thank you. I appreciate your comments and even more so your full report that I hope people will take a look at.

I did note that you mentioned interest rates and confidence in the dollar, and I think they are both tied together, and I have looked at what a difference that will make.

Now we will turn to questions, and to explain the process, each member will have 5 minutes for questions. Normally we would start with myself and then the Ranking Member, but Senator Grassley has been on this Committee longer than I have and could have been the Chair of it several times and has long experience with it. Of course, he is chairing the Finance Committee right now, and this is all related to that. So I will yield my time to Senator Grassley.

Senator GRASSLEY. Thank you for your courtesy. And, Director, I am glad to see you in your new position and have you here.

During Presidential elections, Democrats here in the Senate decide to manufacture some sort of crisis in Social Security. Then they use that crisis to try to scare or mislead seniors, and make the disabled end up believing that some people want to destroy the program. And they feed those scare tactics to whoever is the Democrat nominee for President.

In light of the recent Executive order (EO) to allow an optional deferral of payroll taxes for employees, some Democrats wrote to the Social Security Chief Actuary about some sort of hypothetical legislation that they do not support. The hypothetical legislation would entirely eliminate payroll taxes that fund Social Security. So three questions.

First, are you aware of any plan by anyone to entirely eliminate payroll taxes and destroy Social Security?

Mr. SWAGEL. No, I am not. And I read the SSA Actuary's analysis and saw that he also said that there was no plan that he was aware of either, and it was entirely hypothetical.

Senator GRASSLEY. Okay. Second, can you tell me what effect the President's Executive Order to allow deferral of some payroll taxes for a few months has on the CBO's long-term outlook for Social Security Trust Funds?

Mr. SWAGEL. That EO is not in our figures, just as we closed out our books before—just before the President issued it. But that would have essentially no impact on the long-term budget outlook. It is deferral, not a change in the long-term——

Senator GRASSLEY. Okay. Third, does CBO know that the Treasury Department will continue throughout the year to make deposits in the Social Security Trust Fund associated with payrolls, even with the optional deferral?

Mr. SWAGEL. Yes, that is correct. The Treasury will continue to pay into the trust funds even with the deferral.

Senator GRASSLEY. Then the last one on this subject: According to the Social Security Chief Actuary, the employer payroll tax deferral in the Coronavirus Aid, Relief, and Economic Security (CARES) Act legislation, which enjoyed support of all Democrats and Republicans who voted, does not affect revenue in the trust funds. Do you agree with that assessment?

Mr. SWAGEL. Yes, I do.

Senator GRASSLEY. Okay. Hitting Social Security from a little different angle, CBO's projections for when Social Security Trust Funds are exhausted are different from projection in the Social Security Trustees Report. CBO has also provided estimates for effects of reform bills that differ from estimates that the Social Security Chief Actuary provides as technical assistance. As an example, Representative John Larson has a reform bill called the "Social Security 2100 Act." That bill increases taxes substantially, including taxes for low-wage earners and the middle class, and it also increases Social Security benefits with most of the extra dollars going to upper-wage earners.

The Social Security Actuary estimated that the bill would go a long ways to generate financial sustainability of Social Security. CBO had a different assessment and estimated that the bill would only postpone exhaustion of Social Security Trust Funds by around 9 years. CBO and Social Security Actuaries and Trustees also seem to have different outlooks for when Social Security Trust Funds will be exhausted under current law.

Can you discuss the sources of some of the differences between estimates concerning Social Security programs at CBO and Social Security Actuaries who provide technical assistance?

Mr. SWAGEL. Yes, sir, I can. We have different modeling approaches, but the main difference between our estimates and the Actuaries' estimates are in the parameter choices. So the underlying numbers for fertility, for longevity, mortality, income inequality that have all the economic variables that affect the financial condition of the Social Security system. So we have a bit more pessimistic view. We have the trust fund exhausted in 2031, and before the pandemic, they had it in 2034 or 2035.

Just as an example, after the financial crisis, fertility—so the number of babies for each woman of child-bearing age—did not rebound as much as it had in the past after past recessions. So we have marked down fertility, and that means over 75 years that it is a negative or the Social Security financing system. So that is the sort of difference that we have taken into account. This year the Trustees started to take that into account. We have some other differences on inequality and things like that as well.

Senator GRASSLEY. Thank you, Dr. Swagel.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you, Senator Grassley.

Senator Scott had another Committee meeting that he had to duck into. He will be back. But I will go ahead and ask some questions, and then Senator Kennedy, followed by Senator Toomey, Senator Crapo, and now Senator Braun, in that order, depending on who is online or here.

So to begin my questions, right now the interest on the Federal debt are at historic lows, even negative on an inflation-adjusted basis. I read some claim that means that debt and deficits do not matter. Is that true?

Mr. SWAGEL. No, sir. We would say that they still matter, that the low interest rates, of course, are reducing the cost of servicing the debt, but over time, as the economy recovers, as we get past the pandemic, and as the debt rises, we expect interest rates to rise, and the cost of servicing the debt will become more challenging.

Chairman ENZI. Well, CBO, you projected that interest rates will stay well below what we have seen in the past. The average rate on the 10-year Treasury note over the last 30 years was 4.5 percent, but CBO projections are that it will average about 2 percent between 2020 and 2030. Even still, CBO projects interest spending will skyrocket in the long-term budget outlook.

How would your projection budget change if interest rates were 1 percent higher? What if the rates matched their historical average over the last 30 years? I am asking for some numbers.

Mr. SWAGEL. I know. I understand, I understand. So I will just start by saying we have interest rates staying low as the economy recovers. By 2028, we see the economy back at our potential, past the lingering effects on the economy of the pandemic. Obviously, there are lots of lingering effects. And as that happens, that is when we start to see interest rates rising.

So it could happen sooner, it could happen later. If it happens sooner and more, that would have a very substantial effect on debt-to-GDP, and so just to give the example that you cited, if interest rates were 1 percentage point higher than we forecast, the debt-to-GDP ratio, you know, 30 years out would be something like 254 percent of GDP instead of 195 percent of GDP. So it is a really sizable difference, just 1 percentage point difference in the interest rate.

Chairman ENZI. And what has the historical average for interest rates been in the last whatever number of years?

Mr. SWAGEL. So we looked at the 30-year average, and that is about 4.6 percent for the 10-year, which—you know, of course, it is hard to predict interest rates way out into the future, but we do have historical low interest rates right now.

Chairman ENZI. And they are related to how much people have faith in what we are doing, I think. If they have less faith, they will need more interest in order to leave their money with us. But your updated projections show that the economic downturn has strained the financials of several trust fund programs that were already in trouble. Can you discuss how the CBO's projections of Social Security, Medicare, and Highway Trust Funds have changed and how they are already running deficits?

Mr. SWAGEL. So the trust fund report that we released at the same time with the budget update showed that the Federal trust funds that you mentioned—Highway, Medicare, Social Security disability, and the main Social Security—all have exhaustion dates sooner than we previously expected, and this reflects in large part the effect of the pandemic in reducing the contributions that go into those trust funds. So, each year forward, means that we have less time to address it. The cumulative trust fund deficit that we see over the next 10 years—so, of course, all the trust funds, it is over $2 trillion, $2.3 trillion for 10 years. That is the whole of the trust funds, the net deficit in them over the next 10 years, just as an indication of the challenge that is really in the next decade.

Chairman ENZI. I appreciate your precise answers. I have a few more questions, but I will turn to Senator Braun,

Senator BRAUN. Thank you, Mr. Chairman.

Dr. Swagel, if you remember the last time we were together, I was wanting you to maybe revise what the impact was from the Tax Cut Act of 2017. I think the original amount from your office was that it would have a $150 billion per year impact, $1.5 trillion over 10 years. Is that roughly correct?

Mr. SWAGEL. That is right.

Senator BRAUN. And then I noticed pre-COVID that it looked like we were generating record revenues—is that correct?—in terms of what it was compared to the year before and I think maybe up somewhere in the range of 4 to 4.5 percent.

Mr. SWAGEL. The revenue dollars——

Senator BRAUN. Yes.

Mr. SWAGEL. —was certainly extremely strong. The revenue as a share of GDP was slightly below the long-term average but set to rise up above that long-term average.

Senator BRAUN. But the increase from the last measurable year to the year before has been over 4 percent, hasn't it?

Mr. SWAGEL. Yes.

Senator BRAUN. Okay.

Mr. SWAGEL. We had a strong economy, and it is reflected, as you said, in the revenue figures.

Senator BRAUN. So do you still stick with that projection that over a 10-year period? Now that you have had the benefit of at least a couple years in the trend that we were on pre-COVID, I will give you the opportunity to revise that projection if you want to.

Mr. SWAGEL. We have not gone back and revised that. For sure, the economy before the pandemic was strong, the labor market was strong, and that translated into revenues. The challenge is distilling, you know, that strength of the economy, distilling out the specific effects of the 2017 Tax Act. We have not gone back and done that. You know, we will continue to go back and look at that.

Senator BRAUN. Well, one thing you might do is look at whatever the parameters were when you made it in the first place, and you had to use some method that was going to make that differentiation. I still would like to see that. I know COVID has put a glitch in that.

But let us look at it this way: We have a structural deficit of roughly $1 trillion, COVID aside, correct?

Mr. SWAGEL. That is right.

Senator BRAUN. Okay. So $150 billion divided by $1 trillion is 15 percent, correct?

Mr. SWAGEL. Yes.

Senator BRAUN. So 85 percent of the structural deficit would have nothing to do with the original projection if, in fact, that is still true. So it gets down to whatever we do, and looking at whoever put the chart together on easy pay-fors for Social Security and Medicare—was that you or was that—did you do this, Chairman?

Staff. That is from the Manhattan Institute.

Senator BRAUN. Okay. So have you looked at these? Do you believe them to be accurate?

Mr. SWAGEL. I am sorry. The chart——

Senator BRAUN. Well, we will get you one of these. It is a different——

Mr. SWAGEL. Ah, I know that. I can tell just by looking at it from here. It is Brian Riedl, I think. It is his chart.

Senator BRAUN. Yes.

Mr. SWAGEL. I looked at it very quickly just in the last day or two.

Senator BRAUN. And if you look at what they do over 10 years, some of them being very, very drastic, it still leaves a gap, unless you may be combine a couple of them.

So I think it clearly gets down to the fact that we have a spending issue more so than a revenue one, and I am going to end up with this question, which is two-part: Do you think we have hit the sweet spot of taxation? That is something if you cannot give me an answer today, I would love for you to get back to it. And I think that at some point we have got to realize that whatever we do on the tax side of the equation, it is not going to address the fact that we do not have the political will to do something on the spending side. In general, do you think that is a fair statement?

Mr. SWAGEL. I will cover a couple of these, if that is okay.

Senator BRAUN. Okay.

Mr. SWAGEL. I will start by—at the end of this year, we are going to put out an option—a volume of budget options, so we will—we will not tell you—you will never hear from me what the Congress should do, but we will give you our analysis and sort of our version of that menu, you know, entirely up to you to choose.

At CBO, we think of it as a deficit problem and a debt problem, and not as much of a revenue problem or a spending problem, just because, you know, we shy away from saying what the Congress should adjust. But for sure, as you say, there is a deficit problem, there is a debt problem, and that action is needed. And whether the Congress does it on the spending side or the revenue side, we will provide the analysis, but action is absolutely needed.

Senator BRAUN. Thank you.

Mr. SWAGEL. Okay.

Chairman ENZI. You are doing an excellent job of answering questions concisely, and I appreciate it. I have a few more questions I will do, and if Senator Braun has some more, we do that, too.

Dr. Swagel, you are hardly the first CBO Director to warn this Committee about a dire fiscal outlook. The pandemic has not created the issue. How long has CBO been warning us that the Federal budget is unsustainable?

Mr. SWAGEL. So the first long-term budget outlook came out in 2000, October 2000, and that warned about rising costs for retirement and health care. And that was, of course, even as the budget was in surplus at the time. So at least for 20 years we have been flagging this issue. I suspect Alice Rivlin, the founder of the agency, had it in her mind as well.

Chairman ENZI. I appreciate that, because our soaring debt raises the possibility of a fiscal crisis similar to what we saw in several European countries. I got to visit Greece after that where they impounded personal savings accounts. I have read that it is foolish to worry about a U.S. debt crisis because we are not seeing any warning signals. CBO and most other forecasters do not anticipate particularly high interest rates or inflation anytime soon. Does that mean that we cannot face a debt crisis?

Mr. SWAGEL. No, sir, and that is the challenge, that the financial markets are not flashing those warning signs now. But the reasoning is understandable given the effects of the pandemic and the actions of the Federal Reserve and the situation around the world, where our economy still looks like the most trustworthy in many dimensions.

As the economy recovers, as the Fed normalizes its policy and does not suppress long-term interest rates, and as the debt-to-GDP ratio continues to rise, we worry that all the things holding down rates now will unravel and reverse, and we will have the problem upon us.

Chairman ENZI. Thanks. My last comment and question: Congress used to be governed by an overall principle that you could pass legislation as long as it did not add to the deficit. That was the pay-as-you-go (PAYGO) principle. I think you would agree that when it comes to nonemergency spending, the PAYGO principle is useful. Still, given the current forecast, is PAYGO enough? Or do we need to actively take steps toward deficit reduction?

Mr. SWAGEL. PAYGO is a step, that is for sure, so I do not have negative things to say about PAYGO. The challenge is that PAYGO does not address the existing balance—does not address the existing problem, which is already steep, and there is a sense in which PAYGO actually makes it harder because, of course, any offset, whether on the spending side or the revenue side that is used to pay for the new activities, is no longer available to address the existing imbalance. So as an example, reversing the 2017 Tax Act and then spending it all—right?—that is PAYGO. But that is in some sense the same as if the 2017 Tax Act had never happened and just spending had been raised. So that is the challenge with PAYGO. In a sense it makes things harder.

Chairman ENZI. Well, we have another tactic that we use, which is to borrow future revenue and spend it immediately, and that is not PAYGO either. We did a National Parks bill to cover deferred maintenance here earlier in the year, and people lauded it, and it is a good idea to try and cover that. But I had some suggestions in there for ways that we could actually raise the money. It would have been additional revenue, and most of it would have come from foreign visitors. But I could not even get the amendment up.

Kind of in closing, I will mention that I talked to an inventor, a United States inventor. His name is Dean Kamen. He did the Segways that you see policemen riding around on, and he even invented a wheelchair that would go up and down stairs, but that was after 200 medical patents that he did. Then he got to play with these other things. So he does a lot of thinking, and he got a hold of me about the pandemic things that we were doing and said, "You know, you are actually spending some of that Social Security money, and you are giving out money in the pandemic checks. Why don't you get the people that are receiving that money to sign that they will take a deferral on receiving their Social Security and allow for means testing?" He said, "Particularly young people would probably sign that, and that would help to overcome the deficit."

And I am out of my time here, but I see that Senator Van Hollen is here, and I would give him an opportunity for questions before we close if he wishes. Senator Van Hollen.

Senator VAN HOLLEN. Director, good to have you with us. I had not planned to address this, but since Senator Grassley raised the issue of a letter a number of us sent to the Social Security Actuary, I thought I would address it. And while we indicate in our letter that we were discussing a hypothetical proposal, the reality is that Donald Trump did say—and I am quoting here—"And the payroll tax, we will be terminating the payroll tax after I hopefully get elected." He went on to elaborate on that. So it was appropriate that we asked the Actuary what the impact of that would be on Social Security, and I am sure if you ask folks at the White House whether that is what President Trump meant to say, they will say it is not. But we have also learned that the only person who counts in this White House is the President himself, which is appropriate, and that is what he did say.

With respect to PAYGO, I would just point out that when the big tax cuts were passed in 2017 that disproportionately went to the wealthiest Americans, as part of that, our Republican colleagues waived the PAYGO rule as well as the law, the statutory PAYGO, because, otherwise, the statutory PAYGO rule as well as the law would have constrained that tax cut and would not have allowed another $2 trillion to be added to the deficit.

We are now in the middle of this pandemic right now, and the CARES Act, of course, put forward a number of ways to address it, and I think that bipartisan effort did help rescue many families and small businesses. Interestingly, in your report, at Table 3, you assess the relative benefits of those different approaches. And as I see this, you say that aid to State and local governments is among the most efficient forms of economic stimulus that was passed by Congress. Is that correct?

Mr. SWAGEL. Yes, sir, that is correct.

Senator VAN HOLLEN. I mention that because the Health and Economic Recovery Omnibus Emergency Solutions (HEROES) Act that passed the House I think almost 5 months ago now contains substantial support for State and local governments who are struggling and will otherwise have to lay off workers; whereas, the proposal put forward here in the Senate by Senator McConnell had zero additional funds for State and local governments. So it is interesting to me that that has been determined to be one of the most effective things that we can do going forward.

Similarly, I see under your revenue provisions—and I know it is a mix of them, but collectively you find that some of the tax cut provisions are among the least effective in terms of dollars spent per economic growth gain. Is that correct?

Mr. SWAGEL. Yes, that is correct. And as you said, the State and local money is especially effective in terms of the change in the deficit, how much GDP does it add. It means that States and local governments do not have to raise taxes or cut other spending by as much as they might have to, and that is why we get that result.

The taxpayer provisions do have a positive impact on GDP, but as you said, not as large as the State and local money.

Senator VAN HOLLEN. Right. We are talking per dollar spent, and we have had conversations in this Committee about how we can most efficiently spend, for example, our housing dollars. But what your report shows is that a State and local government expenditure, the spending on health for them, is a lot more efficient per Federal dollar spent than the tax expenditures taken together. Is that right?

Mr. SWAGEL. That is right. That is what our report finds for the money that has been enacted so far.

Senator VAN HOLLEN. Yeah, and just in terms of the public health issue, you have a paragraph here talking about how one of the fastest ways to speed up economic growth and regain ground is to deal with the public health issues, which makes common sense. The more comfortable people are going out about a business and can normalize their activities, the sooner we will get back to that. And you point out that we could reduce the scale of social distancing needed to slow the spread of the virus with more widespread use of masks, greater testing, and increased contact tracing. Is that right?

Mr. SWAGEL. Yes, that is right, and that social distancing would have an effect on the economy and also on the effectiveness of policy; that if Congress puts more money into fiscal policy with less social distancing, the sorts of interventions you mentioned, that money would be more effective, and people would be able to spend more and more rapidly.

Senator VAN HOLLEN. Sure. The more comfortable people feel by applying those measures that have been advocated by the public health experts, the sooner we will get our economy going.

Senator VAN HOLLEN. Thank you, Mr. Chairman, and thank you, Mr. Director.

Mr. SWAGEL. Thank you.

Chairman ENZI. Thank you. If you want to ask some more, you may. I will call on Senator Braun for a second round.

Senator BRAUN. Thank you, Mr. Chairman.

In the modeling that you use to come up with predictions on what raising or lowering taxes would do, I am assuming it is a dynamic system that does reflect that when you raise taxes, it generally as a rule is going to depress economic growth. Do your models incorporate that?

Mr. SWAGEL. Yes, they do, and we look at the details of the tax. So a higher tax on capital, for example, would mean a lower return to investment. We would have less investment. We would have less saving. That would affect the capital stock.

Similarly, a higher tax on wage income would affect people's willingness to work, and that would affect the economy as well.

Senator BRAUN. Well, that is good. I figured the case, and it is leading to a second question, and I will be interested to see if you differentiate between the two kinds of personal income. Before the Tax Act of 2017, I think the highest marginal rate was 39.6 percent, and I think that was applied to W–2 and 1099 income as well as K–1 income. Is that correct?

Mr. SWAGEL. That is correct.

Senator BRAUN. And to me, those are two different kinds of income taxed at the same rate. One is liquid as you can get, W–2 and

1099. K–1, on the other hand, which is called “business income,” “flow-through income,” is inherently illiquid.

Do you differentiate between the two kinds of personal income? Because the rates got separated in the Tax Act of 2017. Is that reflected in your models in terms of what it would do lowering the 1099/W–2 rate versus the K–1 rate?

Mr. SWAGEL. Yes, we would take that into account in our modeling, and we would also take into account the difference between the pass-through rate and the corporate rate, you know, shifting the incentives for a business to decide whether to incorporate or remain a pass-through, all of those.

Senator BRAUN. So has your modeling since then reflected the benefit of basically keeping the 1099/W–2 rate—I think it is at 37 now versus 39.6. Have you been able to measure the benefits into the strong economy that you cited earlier which, anecdotally and theoretically, I would say has been the driver of the recent prosperity pre-COVID? And whenever you are talking about taxing the wealthy, to me that is a liquid income. Most small businesses, whether you are a proprietorship, a partnership, a Sub S, an LLC, you are going to have the K–1 type income.

So it sounds like your modeling reflects that, and that is good to know, and I personally think that has been the driver behind how well the economy has done. And I cite the corporate rate to where I think nominally it was, what, 35 percent prior, 21 now? And my understanding, the effective rate was as low as 18 percent when the nominal rate was 35. Is that your understanding or do you have a different figure on that?

Mr. SWAGEL. I do not have the figure off the top of my head.

Senator BRAUN. I think it is somewhere in that neighborhood, and even though the nominal rate has fallen to 21, the effective rate has only fallen to 16. That shows you how much our Tax Code is littered with write-offs that benefit just some.

A final question would be when it comes to—and you mentioned it earlier, that we are paying almost a zero interest rate when you take into account inflation, is that due to the fact that we are basically the only reserve currency, that others are willing to lend us money of a different currency knowing that it generally will stay put and not depreciate? Is that part of why we are borrowing money so cheaply currently?

Mr. SWAGEL. It is. And it is an extraordinary privilege, is the way economists look at that, that the U.S. has this special position in the global economy.

Senator BRAUN. And is there a risk that if there would become another reserve currency, you could see interest rates spike pretty quickly? I think the euro might have been headed there before they cropped up with Greece and Spain and Portugal and Italy, to name a few. Is that a risk?

Mr. SWAGEL. That would be the risk, that if the U.S. loses its special place, sure, we could co-exist with another currency; but if people lose trust in our economy and our fiscal system, financial system, the effects could be quite rapid.

Senator BRAUN. Thank you.

Mr. SWAGEL. Mr. Chairman, could I mention one more thing just on this line? On the data that we have—the 2018 tax data has only recently become available, and so we are starting to work with that, and, of course, that will show the effect of the 2017 tax cut, the initial effect. So we are working on that. We work on that for distribution, but we will also work on that for the tax policy work that I know you are very focused on. So we will have more to say on this, and we will be happy to talk more.

Chairman ENZI. Senator Van Hollen?

Senator VAN HOLLEN. Thank you, Mr. Chairman. And, Mr. Director, I just wanted to ask you about something that Secretary Mnuchin said on national television earlier this month: "I think before we got into COVID, I thought the debt was very manageable. We were having extraordinary growth. We were creating growth that would pay down the debt over time."

So this question relates to the factual accuracy of that statement and the issue of economic growth and debt. I would first point out that in the first 3 years of the Trump administration, before the pandemic hit, average economic growth was 2.5 percent, 2.5 percent over those 3 years; whereas, in the last term of the Obama administration it was 2.4 percent, one-tenth of a percent. I often hear my Republican colleagues describe the Obama administration years as "no growth," "negative growth," and the Trump years as "supercharged growth." Well, that just is not the case. The facts do not show that.

My question to you relates to the statement where he said we were creating growth that would pay down the debt over time. So a couple factual questions.

First, in 2018 and 2019, before the coronavirus pandemic, was our national debt increasing or decreasing?

Mr. SWAGEL. The national debt before the pandemic was still increasing, absolutely.

Senator VAN HOLLEN. That is right. In fact, as I look at your report and the numbers, it appears that the debt held by the public as a share of GDP was 70 percent in 2017, 77.4 percent in 2018, and 79.2 percent in 2019. Is that what your report shows?

Mr. SWAGEL. Yes, sir, that is right.

Senator VAN HOLLEN. Right. So, clearly, despite what the Secretary said, the debt was going up. The growth was not sufficient to be reducing the debt.

Second, in CBO's January 2020 budget projections, which you published before the coronavirus pandemic hit in the United States, did CBO project that our national debt would increase or decrease over time?

Mr. SWAGEL. So we had the debt trajectory continuing to increase. Instead of, you know, the $1 trillion deficit, we projected—before the pandemic it was extremely high by historical standards, even as the economy was growing and the labor market was strong before the pandemic.

Senator VAN HOLLEN. Right, so I appreciate that. So it is just not factually correct that we were creating growth that would pay down the debt over time, is it?

Mr. SWAGEL. That is right. We did not expect the pre-pandemic economic situation to lead to paying down the debt.

Senator VAN HOLLEN. And now, of course, we have an even bigger hole to dig out of. Is that right?

Mr. SWAGEL. That is right.

Senator VAN HOLLEN. Although if we were not taking action to compensate for all the people who are out of work in the small businesses, the hole might get even bigger. Isn't that right?

Mr. SWAGEL. Certainly the economic situation would be much more difficult without the actions taken by the Congress helping families, businesses, schools, children, a wide variety. Absolutely, the situation would be—the economic situation and the social situation would be much more difficult.

Senator VAN HOLLEN. Yeah. Thank you, Mr. Director.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you. Thanks for participating in the hearing. And, of course, we had the housing hearing last week, and there appeared to be a lot of agreement on what could be done. Of course, the devil is always in the details, but that was one of the first positive hearings that I have been to in a long time.

I want to thank Dr. Swagel for his appearance before the Budget Committee today, for the work that he and all of his people have done to provide us with this information, which is quickly changing information.

As for the information for all the Senators, questions for the record are due by 12:00 p.m. tomorrow. Emailed copies of the questions are acceptable due to the current conditions. Under our rules, Dr. Swagel will have 7 days from the receipt of our questions to respond with answers.

With no further business to come before the Committee, the hearing is adjourned.

[Whereupon, at 3:20 p.m., the Committee was adjourned.]

ADDITIONAL COMMITTEE QUESTIONS

[The following submitted questions were not asked at the hearing but were answered by the witness subsequent to the hearing:]

Congressional Budget Office

DECEMBER 18, 2020

Answers to Questions for the Record Following a Hearing Conducted by the Senate Committee on the Budget on CBO's Budget Projections

On September 23, 2020, the Senate Committee on the Budget convened a hearing at which Phillip L. Swagel, the Congressional Budget Office's Director, testified about the agency's report The 2020 Long-Term Budget Outlook.[1] *After the hearing, four members of the Committee submitted questions for the record. This document provides CBO's answers. It is available at cbo.gov/publication/56908.*

Senator Grassley

Question. In mid-July, Social Security's chief actuary was discussing the Average Wage Index used to help compute Social Security benefits, which may decline this year.

The chief actuary said that experience up to that point for 2020 suggested that total wages for the entire year will be on the order of 10 percent lower than what was projected in the 2020 Social Security trustees report.

And, the number of workers without any earnings received in 2020, regardless of how much they worked in 2020, will be about 1 percent lower than projected in the trustees report.

Data used to compute the Average Wage Index come from tax information collected by the Social Security Administration (SSA), and most of that data, as I understand it, won't be known until late next year.

Director Swagel, I have a few questions about the Average Wage Index, or AWI. Does the CBO have access to data used by SSA to compute the AWI?

Answer. The Congressional Budget Office receives access to data SSA uses to compute the average wage approximately a year after SSA has published the AWI; even then, CBO only gains access to data for a subset of the population (whereas the AWI computation is based on data for the full population). Therefore, CBO's assessments about the 2020 AWI are made from other, similar data sources, such as employer and household surveys, aggregate wages as reported by the Bureau of Economic Analysis, and data on tax withholding.

Question. If so, do you agree with the chief actuary's assessment that as of mid-July, it looked like the AWI will be 10 percent lower than was projected in the 2020 Social Security trustees report, and the number of workers 1 percent lower than projected?

Answer. CBO's current projections of the AWI are based on economic projections released in July. In those projections, the number of people working during at least part of 2020 was

1. See Congressional Budget Office, *The 2020 Long-Term Budget Outlook* (September 2020), www.cbo.gov/publication/56516.

only slightly lower than the agency anticipated in January, but total projected earnings were substantially lower because of the 2020 coronavirus pandemic. As a result, CBO projected in its September report on the budget outlook that the AWI will be about 7 percent lower in 2020 than it estimated at the beginning of this year. The labor market recovery has proceeded faster than anticipated when that projection was made, suggesting that the decline in the AWI will probably be considerably less than the 7 percent projected in September. CBO will release an updated analysis early next year.

Question. And, if you have access to the data, or any data that could help forecast the AWI, how has that assessment changed, if at all, since mid-July?

Answer. Broadly speaking, the labor market rebound has been stronger than CBO anticipated; workers' earnings have come in stronger than CBO anticipated in July, which suggests that the decline in the AWI will probably be considerably less than the 7 percent projected in September. CBO will release an updated analysis early next year.

Question. Social Security's chief actuary has added commentary in the last seven annual trustees report about trust fund accounting versus unified budget accounting.

According to the actuary, under trust fund accounting, benefits can't be paid in full after a trust fund is depleted. In contrast, he says that unified budget accounting assumes full scheduled benefits would be paid with general fund transfers.

The actuary says that draws from the general fund are not permissible under current law, and that—quote—"no precedent exists for a change in the Social Security Act to finance unfunded trust fund obligations with such draws on other Federal resources."

But if I remember correctly, during the Obama administration there were payroll tax holidays where general fund resources were transferred to Social Security's trust funds to help pay benefits. So, I'm not so sure why Social Security's chief actuary continues to make a big deal about trust fund versus unified budget accounting.

Director Swagel, while Social Security does not by itself have borrowing authority, when Congress decides to replenish trust funds with general fund transfers, as was done during the Obama administration, is there any real difference between what the actuary calls the trust fund perspective and the unified budget perspective?

Answer. Whether benefits are financed by Social Security taxes or by general fund transfers to the trust funds makes no difference to recipients of those benefits—the distinction between the trust fund perspective and the unified budget perspective does not affect the amount received by Social Security recipients if the Congress replenishes trust funds with general fund transfers.

CBO projects that the Social Security trust funds will be exhausted in coming years. Upon exhaustion and without legislative action, benefits would be reduced to the amount available from contemporaneous income. But as long as a trust fund's balance remains positive, benefits are paid as scheduled under law. Thus, general fund transfers would delay or prevent trust fund exhaustion and enable payment of additional benefits. Ultimately, the balances of the trust funds are not affected by such transfers because the increased income from the transfers is offset by benefit payments greater than those possible under current law (unless the transfers are larger than needed to pay scheduled benefits).

Such transfers affect the overall federal budget: The additional benefits enabled by general fund transfers would increase the unified budget deficit in years after a trust fund would have otherwise become exhausted, increasing the federal debt relative to what would occur without such transfers (assuming that the transfers are not offset by actions that would increase federal revenues).

In keeping with section 257 of the Balanced Budget and Emergency Deficit Control Act of 1985, CBO's baseline incorporates the assumption that scheduled payments will continue to be made in full after a trust fund has been exhausted, although there is currently no legal authority to make such payments. This means that the additional spending associated with such transfers from the general fund would not be added to CBO's baseline and would not appear in cost estimates for legislation authorizing such transfers (even though the transfers involve a commitment of funds and thus correspond to a use of economic resources by the nation).

Senator Johnson

Question. Current law states if an individual has an offer of "affordable" employer coverage—defined as requiring out-of-pocket premium payments of less than 9.78% of income—they cannot receive a federal subsidy for an Exchange plan. In July 2020, the Biden campaign put forth a list of recommendations which included repealing this policy, referred to as a "firewall" between employer and Exchange coverage. A recent study found that repealing the current firewall, along with richer Exchange subsidies, could cause approximately 24 million individuals to switch to subsidized Exchange plans, leading to $2.2 trillion in new spending on Exchange subsidies. Has CBO studied the impact of – or provided guidance to Congress about a policy—repealing the ACA's firewall and allowing individuals to choose between ESI and individual market plans on the Exchange? If so, what was that analysis or guidance? If not, how would CBO view such a policy?

Answer. CBO has not completed a comprehensive quantitative analysis of the effects of repealing the Affordable Care Act's (ACA's) firewall and allowing individuals to choose between employment-based coverage and subsidized marketplace coverage.

CBO anticipates that repealing the firewall would result in more workers declining employment-based coverage in favor of marketplace coverage. Employers would respond differently to the repeal of the firewall depending on the composition of their workforce and the availability of premium tax credits to their employees: Some employers would rescind insurance offers (because some employees would gain access to better alternatives to employment-based insurance), and some employers would newly offer insurance (because such offers would no longer prevent employees from receiving marketplace subsidies). CBO expects that the combined effect of employees' and employers' decisions would be a decline in enrollment in employment-based coverage.[2]

The impact of such a policy would depend on other components of the legislation, particularly the availability and generosity of marketplace subsidies for workers who are not eligible for subsidies under current law.

Question. Can CBO quantify the change in ESI take-up in the event the firewall gets repealed? Can CBO quantify how much federal spending on Exchange subsidies would increase if the firewall is repealed?

2. For additional discussion of CBO's qualitative assessment of the effects of repealing the firewall on employer decisions to offer health insurance, see Congressional Budget Office, *Policies to Achieve Near-Universal Health Insurance Coverage* (October 2020), www.cbo.gov/publication/56666.

Answer. Although CBO has not produced an estimate for a policy to remove the ACA's firewall, the agency can provide some information from its September 2020 baseline estimates for context.

- CBO estimates that under current law, about a quarter of the 151 million people projected to have employment-based coverage in 2021 would be eligible for subsidies in the marketplaces if the firewall was removed. The newly eligible individuals would be people with income below 400 percent of the poverty level who are not eligible for Medicaid or the Children's Health Insurance Program (CHIP), who currently have an affordable offer of insurance, and who are not immigrants that are not lawfully present.

- The out-of-pocket premium cost for the benchmark plan (the cost used to determine marketplace subsidies) would be lower than the current premium contributions for employment-based coverage for 20 percent of newly eligible individuals. In addition to premiums, a person's choice of insurance plan is also influenced by factors such as total out-of-pocket costs, provider networks, and covered benefits. For individuals and families with income above 250 percent of the federal poverty line, a silver plan purchased through a marketplace would result, on average, in higher out-of-pocket costs, narrower provider networks, and fewer covered benefits than an employer's plan. Consequently, many people who would be made eligible for premium subsidies would choose to remain in an employer's plan.

- People who would be most likely to enroll in marketplace coverage as a result of the elimination of the firewall—people for whom the after-subsidy premium for marketplace insurance would be lower than for employer-based insurance—would be eligible for an average of $4,700 in premium tax credit subsidies in 2021.

- Under current law, individuals who would become eligible for subsidized marketplace coverage by removal of the firewall will receive an estimated tax benefit averaging about $2,000 for their employment-based premiums in 2021. That benefit includes the exclusion of most premium contributions from employees' income taxes and payroll taxes as well as their exclusion from employers' payroll taxes. Employees who would enroll in marketplace coverage instead of employment-based insurance if the firewall was removed would no longer receive those benefits; that reduction in tax benefits would partially offset the federal government's added costs for premium subsidies.

Question. Does CBO believe that employers whose workers voluntarily switch to the Exchanges would receive an increase in taxable wages roughly equal to the cost of the (foregone) employer contribution toward coverage?

Answer. CBO and the staff of the Joint Committee on Taxation (JCT) expect that most of employers' savings would be passed on to workers in other forms of compensation, but not every employee would receive an increase in compensation equal to the amount his or her employer saved for two reasons. First, some of the employers' savings would accrue as increases in profits. Second, any compensation returned to workers would be distributed unequally among workers. How the compensation was distributed would depend on the tightness of the labor market and who was probably most affected when the employer stopped offering insurance. For example, since low-wage employees would, on average, receive larger subsidies for nongroup insurance, it is possible that employers would increase wages less for their lower-wage workers.

Some of the reduction in employers' payments for health insurance contributions that was passed back to their workers in other forms of compensation (such as wages or retirement benefits) would lead to an increase in federal revenues. Additionally, any of the employers' savings that accrued as profit increases would generally be taxed, which would also increase federal revenues.

Question. Does CBO believe that repealing the firewall would cause adverse selection problems between Exchange and employer coverage? If so, which way does CBO believe the adverse selection problems would lie—would sicker individuals tend to remain in employer coverage, or gravitate towards the Exchanges?

Answer. Whether there was adverse selection—a disproportionate shift of people with large expenditures on health care into either the nongroup market or employment-based coverage—would depend both on employers' decisions to offer insurance and on individuals' decisions to purchase coverage in the nongroup market. It is possible that employers would respond to removal of the firewall by encouraging less healthy employees to enroll in marketplace plans by offering less generous benefit packages. Nevertheless, in CBO's assessment, removal of the employer firewall is unlikely to result in adverse selection, in part because out-of-pocket premiums for employment-based coverage and subsidized marketplace plans do not depend on an individual's age or underlying health status. Out-of-pocket premiums instead depend on an individual's marginal tax rate, in the case of employment-based coverage, and on an individual's income relative to the federal poverty level, in the case of subsidized marketplace plans. In addition, average employer contributions are large enough to encourage employees to participate regardless of their health status, and subsidies in the nongroup market are sufficient to attract both healthy and unhealthy individuals. Therefore, CBO expects that both markets would continue to attract a sufficient number of relatively healthy people to maintain market stability.

Senator Warner

Question. In CBO's September report, "The Effects of Pandemic-Related Legislation on Output," CBO estimated that increased funding for state and local governments would boost GDP by 78 cents for every dollar of budgetary cost from FY20 through FY23. Given this rate of return compared to other policies, would Congress passing more assistance for state and local governments generate more economic growth? How would the amount of state and local funding provided by the House-passed *HEROES Act* impact economic growth?

Answer. CBO estimated that the $150 billion in direct assistance for state and local governments provided by the Coronavirus Aid, Relief, and Economic Security (CARES) Act will boost gross domestic product (GDP) by 88 cents per dollar of budgetary cost from fiscal year 2020 through fiscal year 2023. In CBO's estimation, that assistance will boost GDP by 0.5 percent in 2020 and by 0.2 percent in 2021.

The agency also estimates that more support to state and local governments would further boost GDP in the short term by reducing the size of the tax increases and spending cuts that will be required for many state and local governments to balance their budgets. To the extent that it adds to federal deficits and debt, such support could cause the nation's output to be lower than what it would otherwise be in the long term.

CBO has not fully analyzed the effects of the $915 billion in additional funding for state and local governments that would be provided by H.R. 6800, the Health and Economic

Recovery Omnibus Emergency Solutions (HEROES) Act, as passed by the House of Representatives on June 1. CBO's assessment of the effects on GDP from funding for state and local governments in that act would differ from its assessment of the effects of the CARES Act. For example, the outlays from the funds provided by the HEROES Act would probably occur when social distancing restrictions are less stringent, and therefore the positive effects on output per dollar of stimulus would probably be larger than the positive effects of the CARES Act funding. On the other hand, the HEROES Act would provide substantially more funds and states would have greater flexibility in using them than those provided by the CARES Act; states might choose to use them to postpone tapping into their rainy day funds or increasing taxes. If funds provided by the HEROES Act were used in that way, they would have a smaller effect per dollar on GDP than the funds provided by the CARES Act, which state and local governments largely used to increase purchases of goods and services.[3]

Question. State budget shortfalls for FY21, which began on July 1 for most states, are deeper than the shortfalls faced during the Great Recession. Would the existing assistance Congress has passed be sufficient to cover those projected shortfalls? How many states have lost state and local government jobs during the pandemic? If state and local job layoffs persist or the rate of employment growth for state and local governments continues to be slow, what impact would that have on GDP and the U.S. long-term economic recovery?

Answer. The pandemic and associated social distancing measures have had a significant impact on the finances of state and local governments by reducing current and projected tax revenues and creating additional demands for spending. CBO estimates that the direct assistance provided by pandemic-related federal legislation will be disbursed to state and local governments during calendar year 2020. Most of that assistance was provided for specific purposes and will amount to less than state and local governments lose in tax revenues this year.

According to information from the National Conference of State Legislatures (NCSL), most states have enacted legislation to appropriate additional funding for coronavirus-related tasks. NCSL reports that 13 states have drawn money from their reserves ("rainy day funds") and 30 states have instituted across-the-board budget cuts.

State and local government employment declined by 13,000 in November and was 1.3 million (or 6.8 percent) below its February level. If state and local government layoffs persist or if job growth is muted, state and local government purchases of goods and services—which accounted for roughly 11 percent of GDP in 2019 and was primarily the compensation paid by those governments to their employees—would not quickly recover to its pre-pandemic level.[4] A decline or slow growth in real (inflation-adjusted) state and local government purchases would slow the economic recovery.

3. The HEROES Act, H.R. 925, as passed by the House of Representatives on October 1, 2020, would also provide additional funding for state and local governments. CBO's analysis of that provision would be similar to the analysis of the provision in H.R. 6800.

4. In the national income and product accounts, the Bureau of Economic Analysis (BEA) reports government spending in three ways: government purchases (which BEA officially refers to as government consumption expenditures and gross investment), government current expenditures, and total government expenditures. For more information, see Bureau of Economic Analysis, "BEA Seems to Have Several Different Measures of Government Spending. What are They for and What do They Measure?" (May 28, 2010), www.bea.gov/help/faq/552. State and local governments' purchases have been about three-quarters of their total spending over the past few years. State and local governments' total spending includes some items, such as Medicaid expenditures, that are not included in state and local governments' purchases but are instead transfers to people.

Question. Varying estimates, including CBO's, have projected the 2017 Tax Cuts and Jobs Act would add close to $2 trillion to the U.S. national debt. Does the recession the U.S. is experiencing due to COVID-19 impact those estimated costs of the 2017 tax cuts?

Answer. In April 2018, CBO estimated that the tax act would increase the deficit by $1.9 trillion over the 2018–2028 period. That estimate considered all changes to revenues and outlays, including the effects of macroeconomic feedback and changes in debt-service costs.[5]

CBO has not updated those estimates nor has the agency done a comprehensive analysis of how the recent economic downturn or the subsequent legislative changes would affect the estimates. However, the CARES Act temporarily suspended several provisions of the 2017 tax act that would have reduced the deficit had they remained in effect. Those provisions relate to the way businesses can use net operating losses to offset taxable income. Changes that CBO has made to its economic forecast would also affect the estimated costs of the tax act. Recessions tend to reduce the budgetary costs of provisions that reduce taxes because the incomes on which those taxes are levied are generally smaller. In addition, the decline in interest rates that has occurred since the onset of the coronavirus pandemic will reduce the government's cost of servicing the national debt.

Question. How much has the TCJA added to the national debt?

Answer. In April 2018, CBO projected that the 2017 tax act would increase the deficit by $1.9 trillion over the 2018–2028 period; that estimate included the effects of macroeconomic feedback and changes in debt-service costs. Those cumulative annual deficits were anticipated to total $664 billion through fiscal year 2020.[6] CBO has not subsequently updated those estimates.

Although information is now becoming available from tax returns filed for the 2018 tax year—the first returns that reflect most of the changes made by the tax act—assessing the act's effects on overall receipts in a comprehensive manner is challenging. Many other factors influence economic growth and thus alter receipts, including changes in trade policies implemented by the Administration that have tamped down business investment and economic growth, the economic effects of the pandemic, and the government's response to it. It would be difficult to disentangle the impacts of the tax act from these subsequent developments.

Question. How much is the TCJA projected to add if the expiring provisions are extended?

Answer. All revenue estimates of proposed tax law changes are provided by the staff of the JCT. As part of CBO's report *An Analysis of the President's 2021 Budget*, JCT estimated that extending certain provisions of the 2017 tax act that are set to expire in 2025 would increase cumulative deficits by $1.2 trillion through 2030.[7] However, those estimates were completed before the onset of the economic disruption caused by the pandemic and actions taken by the government in response.

5. See Congressional Budget Office, *The Budget and Economic Outlook: 2018 to 2028* (April 2018), Appendix B, www.cbo.gov/publication/53651.
6. Ibid.
7. See Congressional Budget Office, *An Analysis of the President's 2021 Budget* (March 2020), www.cbo.gov/publication/56278.

Question. Did the deficit-financed tax cuts put us in a stronger position to respond to this recession?

Answer. Although the 2017 tax act increased budget deficits, policymakers currently have the ability to use fiscal policy to respond to the recession (in addition to the CARES Act and other legislation enacted so far). The 2017 tax act has ongoing effects on the economy. The effects of the changes that act made to corporate and personal tax rates that boost the productive potential of the U.S. economy (including higher investment spending and increased labor supply) will continue through the recovery and subsequent expansion. However, the personal tax cuts in the law are scheduled to expire after 2025. Depending on the state of the economy at that time, the expiration of those tax cuts might have negative effects on the economy (such as reduced overall demand and output) in the short term, but positive effects (because of smaller deficits) in the long term. In addition, the larger deficits and debt caused by the act may constrain policymakers' choices in the future.

Question. Does CBO expect a "K-shaped recovery" from COVID-19, where higher-income Americans see a close to full or full recovery and lower-income Americans are left behind? How has the inflation rate of certain categories of goods impacted low-income Americans? For example, would rising prices of groceries have a disproportionate impact on Americans with less wealth? If Congress pursues another COVID-19 relief package, what is the most cost-effective policy Congress can pursue that would also address the situation facing low-income Americans?

Answer. The recovery from the 2020 recession could look different than the previous two recoveries (those starting in 2002 and 2009) because the nature of the most recent downturn was very different than the previous two. First, in those recessions, the contraction of activity was distributed widely across the economy and lasted for much longer. The most recent recession, however, was very deep but short, and its negative effects were concentrated in occupations and industries with large shares of low-wage jobs. Second, during the previous two recessions, higher-income households experienced the greatest proportional losses to income, but those same households also saw the largest gains in recovery. By contrast, lower-income households have borne the brunt of the impact of the pandemic and the subsequent recession, in terms of both health and economic effects.[8] Early data indicate that, on average, higher-income households remain relatively less affected.

Because the 2020 recession affected people at different income levels differently, the recovery period is also likely to differ for higher-income and lower-income people. The shape of the recovery for low-income households will depend on many factors, especially the course of the pandemic and the structural economic changes that might occur because of it. Persistent changes in the demand and supply of different services may require the reallocation of workers and capital within and among companies, industries, and regions. On the one hand, for example, if the travel and tourism industries suffer a permanent reduction in demand, the burden of adjustment—lower employment and income—will fall on the workers and the regions most affected. On the other hand, the pandemic could recede more quickly (perhaps because of a vaccine) and structural dislocations could turn out to be minor. Compared to the two previous recoveries, growth in employment and wages might be more rapid, which would reduce the negative consequences of the pandemic for low-income households.

8. Specifically, the largest job losses occurred in low-wage service industries, such as leisure and hospitality and retail sales, which require a high degree of in-person contact. Of those workers who retained their jobs in such industries, lower-wage workers occupied a disproportionate share of the jobs that involve elevated risks of exposure to the coronavirus.

Other pandemic-related problems pose risks to the long-term well-being of lower-income people:

- Adapting to changes in the economy may be costly and take a period of years. In labor markets, that slow process of adjustment might increase unemployment rates for an extended period and so weaken the bargaining position of workers.

- The difficulties associated with juggling intermittent income and childcare are especially acute for lower-income households with school-age children (especially single-parent families) and those with uneven access to affordable health care.

- Children from lower-income households will be more likely to suffer from hunger and malnutrition and lose access to meaningful schooling, particularly in areas where schools are operating remotely. The harm of remote schooling is skewed disproportionately to children who are already most disadvantaged in our society.

Additionally, since lower-income Americans spend a larger share of their income on food, they would be particularly affected by a large increase in the price of groceries relative to other goods. The price of groceries rose considerably more rapidly than the prices of most other goods in the first few months of the pandemic, which potentially added to the unequal burden borne by lower-income families. However, that spike in grocery prices was concentrated in the prices of a few goods, such as beef, so some families may have substituted for those items with other lower-cost products. Grocery prices have fallen from their peak in June, and CBO expects only modest growth in grocery prices over the next several quarters.

Fiscal policy can provide a safety net to help lower-income households. In the current situation, unemployment benefits and direct transfers of cash targeted at low-income households can most help such households. In the long term, the prospects for economic growth and its distribution are uncertain, and the effects of any policy will depend on its design and implementation.

Question. Does Congress' failure to renew expiring COVID-19 relief programs threaten to undo the stimulus effect of the programs or exacerbate the economic damage caused by COVID-19?

Answer. The expiration of pandemic relief programs will lead to slower growth and a weaker job market in early 2021. CBO analyzed expiring coronavirus relief programs in its September report *The Effects of Pandemic-Related Legislation on Output*.[9] The agency estimated that by providing financial support to households, businesses, and state and local governments, those programs will raise real GDP this year and next. However, those programs will reduce the level of real GDP in the long term (because of the larger federal debt).

In CBO's assessment, additional legislation that followed the same broad contours of the expiring relief programs would have similar effects, although the degree to which output was affected in the short term would depend on a number of factors, including the precise parameters embedded in the legislation and when it was enacted. The effects would also depend on the size of the stimulus: A very large stimulus might result in diminishing returns in the short term.

9. See Congressional Budget Office, *The Effects of Pandemic-Related Legislation on Output* (September 2020), www.cbo.gov/publication/56537.

Question. How much money has President Trump's four executive orders (i.e., payroll tax deferral, student loan deferral, housing assistance, and disaster benefit assistance/unemployment compensation) provided to American households? How does the $44 billion in disaster relief funds provided by the Trump Administration compare to the additional $600-a-week jobless benefits established by the *CARES Act*, both in terms of dollar amount and impact on economic growth?

Answer. The President's actions allowed use of up to $44 billion in disaster relief funds for unemployment benefits; to date, about $36 billion of that total has been spent. CBO estimates that outlays for Federal Pandemic Unemployment Compensation (FPUC), which provided additional benefits of $600 per week of unemployment to unemployed people through July 2020, will total $291 billion.[10] The agency also estimates that the net effect of those enhanced unemployment benefits will be to boost GDP by 67 cents for each one-dollar increase in budgetary cost.[11]

The President also deferred payments, interest accrual, and involuntary collections on certain federal student loans through December 31, 2020. Changes to the student loan program are recorded on a present-value basis (pursuant to the Federal Credit Reform Act of 1990); the Administration has recorded a cost of $14.6 billion for those deferrals.

In addition, the President allowed employers to defer withholding and payment of workers' payroll taxes for Social Security from September 1 to December 31, 2020, for workers generally making under $104,000 per year. That action changed the timing of some tax payments but not the amounts owed. CBO has not estimated the effect of the executive action on revenues but does not expect it to have a significant effect on the agency's next revenue baseline projection.

The President also directed federal agencies to consider actions they could take to prevent evictions. The Centers for Disease Control and Prevention responded by issuing an order that temporarily halted evictions of covered people from residential properties for nonpayment of rent through the end of the year. The executive order provided no additional budgetary resources.

Question. As Congress negotiated and passed coronavirus-related relief legislation in March and April, foremost in our minds was the health and safety of our constituents and bolstering American families with the economic resources needed to weather this ongoing crisis, not concerns about propping up Gross Domestic Product. As the CBO points out in its September report "The Effect of Pandemic-Related Legislation on Output": "In addition to affecting overall economic activity as measured by real GDP, the legislation will affect other important aspects of the economy and people's well-being." Critical among the efforts in our coronavirus relief measures were extended unemployment benefits to help the over 61 million Americans, including 1.4 million Virginians, who have filed initial claims for unemployment since the pandemic began. The expanded federal assistance has made all the difference for millions of Americans in keeping food on the table, being able to pay rent, and affording prescription drugs. The CBO asserts that several factors complicate analysis of whether enhanced unemployment compensation disincentivizes work and output, namely high unemployment and social distancing.

10. See Congressional Budget Office, *An Update to the Budget Outlook* (September 2020), www.cbo.gov/publication/56517.

11. See Congressional Budget Office, *The Effects of Pandemic-Related Legislation on Output* (September 2020), www.cbo.gov/publication/56537.

Have you seen any evidence to contradict Yale's Tobin Center for Economic Policy's July finding of "no evidence that more generous benefits disincentivized work either at the onset of the expansion or as firms looked to return to business over time?" Since Pandemic Unemployment Assistance (PUA) expired in July, have you seen greater gains in employment for workers whose enhanced UI benefits were more generous or has it remained consistent across wage levels? Have you seen evidence of decreased consumption spending in the economy overall?

Answer. The Yale study reflected a mix of supply and demand effects and focused on the earliest days of the pandemic shock through early May, which largely predates the reopening of most states.[12] CBO considers its general findings to be broadly consistent with the agency's view of the events that occurred in the early stages of the pandemic.

As states have reopened since May, the generosity of the unemployment compensation may have discouraged some furloughed or laid off workers from returning to the workforce—the Yale study would miss that trend because of the limitations of the data it considers. For example, the Beige Book released by the Federal Reserve Board in July reported that "[c]ontacts in nearly every District noted difficulty in bringing back workers because of health and safety concerns, childcare needs, and generous unemployment insurance benefits."[13] The May report contained similar language. The latest Beige Book (released in September) noted that "[f]irms continued to experience difficulty finding necessary labor, a matter compounded by day care availability, as well as uncertainty over the coming school year and jobless benefits."[14] In addition, the Census Bureau's Small Business Pulse Survey shows that in August and September, 8 to 9 percent of small businesses surveyed reported that their operating capacity was affected by their "ability to re-hire furloughed or laid off employees and/or hire new employees."[15]

Overall, when forming its views on the likely effects of the CARES Act's unemployment insurance provisions over a longer time horizon, CBO relied on a large body of pre-existing literature in economics and on current research (including the Yale study), which vary significantly in data sources, methodology, and time frame of the analysis. The earlier literature tended to find that increased unemployment insurance payments reduced labor supply—although in times of severe economic downturn, CBO expects that the negative effect on employment will be partially or even fully offset by the positive effect of those payments on the demand for labor.

In the current context, it is particularly difficult to assess the impact of the generosity of the unemployment compensation on labor supply because of the health risks posed by the pandemic and other confounding factors such as the lack of childcare. It is also unclear how much the expiration of enhanced unemployment benefits has affected employment among people at different wage levels. Complex effects of the other government programs—such as

12. See Joseph Altonji and others, *Employment Effects of Unemployment Insurance: Generosity During the Pandemic* (Tobin Center for Economic Studies, July 2020), https://tinyurl.com/y3mkataz (PDF, 2 MB).

13. See Federal Reserve District, *The Beige Book: Summary of Commentary on Current Economic Conditions* (July 2020), p. 1, https://go.usa.gov/x7S5J; and *The Beige Book: Summary of Commentary on Current Economic Conditions* (May 2020), p. 1, https://go.usa.gov/x7S5t.

14. See Federal Reserve District, *The Beige Book: Summary of Commentary on Current Economic Conditions* (September 2020), p. 1, go.usa.gov/xArMt.

15. See Census Bureau, "Small Business Pulse Survey" (October 15, 2020), https://portal.census.gov/pulse/data/#weekly.

the Paycheck Protection Program—on employment have also complicated data interpretation in recent months.

Federal Pandemic Unemployment Compensation, which provided additional benefits of $600 a week, expired in July (although some people continued receiving an add-on to their unemployment benefits through lost wages supplemental assistance funding). Since FPUC's expiration, CBO has not seen convincing evidence of a decrease in consumption spending in the economy overall. However, there has been a slowdown in the *growth* of overall consumption spending. Both official data and new, timelier but more variable, real-time indicators of consumer spending have confirmed that the gains in consumer spending have been smaller in each successive month since June. The observed slowing in the growth of consumer spending is broadly similar to what CBO built into its July current-law projections, which reflected the assumption that FPUC would expire in July. The main reason that CBO expected the growth of overall consumer spending to slow is because, without a vaccine, recovery in many types of service activities is constrained by continued social distancing. In addition, CBO anticipated that reduced income due to expiring programs would limit the spending of affected households, most particularly of people who are unemployed.

Question. In CBO's report discussing effects of pandemic-related legislation on output and enhanced unemployment benefits, CBO mentions the complicating factor of workers' legitimate, grounded fear of contracting and transmitting COVID-19 as depressing output. Specifically, CBO stated: "All of these efforts are complicated by the extent of social distancing and the fact that workers considering a return to work may weigh the risk of increasing their exposure to the coronavirus. That could result in employers' offering higher wages than they would have otherwise, which would reduce the effect of enhanced unemployment benefits on work incentives and ultimately on output." While workers often merit higher pay, the U.S. needs to fundamentally address the root cause of fears surrounding COVID-19: that many workplaces are not safe. Virginia has adopted first-in-the-nation, enforceable workplace safety standards for COVID-19, mandating sanitation, face covering, social distancing, and notification protocols to prevent the spread of COVID-19. To that end, would a nationwide, emergency workplace safety standard help return higher levels of output?

Answer. CBO has not analyzed the effect of changes in workplace safety standards on GDP; such an effect would depend on how the standards were designed and implemented. Economic growth during the pandemic depends in part on employees' willingness to work in the face of the current health risks and in part on employers' willingness and ability to provide safe working conditions for their employees. Steps that made people feel safer working during the pandemic would therefore enhance economic growth. A nationwide standard is one possible step of that type.

Senator Whitehouse

Question. In January 2020 CBO projected that federal health spending over the next decade will be $4.7 billion lower than your 2010 estimates extrapolated out to this budget window. Would you agree that comparing CBO's 2020 baseline with the 2010 baseline extrapolated out to the current window is a logical way to estimate changes in health projections?

Answer. Comparing a 2010 baseline with a 2020 baseline is complicated. In CBO's baseline projections from August 2010—the first projections published after the enactment of the ACA—only one year, 2020, overlaps with CBO's August 2020 baseline projections.

Therefore, a straightforward comparison of the two baselines is possible only for that year. In its August 2010 projections, CBO estimated that mandatory spending for the two broad budget categories covering the major health care programs—function 550 (Health, mostly Medicaid) and function 570 (Medicare)—would be $1,489 billion in 2020. In CBO's August 2020 baseline projections, the agency estimated that such spending would total $1,296 billion in 2020, or 13 percent less than the amount CBO projected in 2010.

CBO classifies changes in its baseline projections in three categories: legislative changes, which result from the enactment of new laws; economic changes, which stem from updates to the agency's economic forecast; and technical changes, which reflect all other updates to the agency's projections. The $192 billion difference between the two federal health care projections for 2020 is the net effect of a $220 billion reduction due to economic and technical changes and a $28 billion increase due to legislative changes. The largest technical revision that CBO incorporated into its August 2020 baseline projections of federal health spending was the slowdown in health care spending growth; however, there were many other technical revisions. For example, CBO also reduced its projections of subsidies provided through the Affordable Care Act marketplaces because the actual number of people receiving subsidies was smaller than anticipated.

One way to extrapolate the August 2010 projections over a longer period of time is to use projections from CBO's 2010 *Long-Term Budget Outlook*, which includes those of federal outlays for major health care programs through 2035.[16] (Outlays for major health care programs consist of spending for Medicare, Medicaid, and CHIP, as well as outlays for premium tax credits and related spending associated with the health insurance marketplaces.) In those long-term projections made in 2010, CBO estimated that federal outlays for major health care programs would increase from 6.9 percent of GDP in 2020 to 8.7 percent of GDP in 2030. In its August 2020 baseline projections, the agency projected that federal outlays for major health care programs would increase from 6.1 percent of GDP in 2020 to 6.9 percent of GDP in 2030. (Nominal GDP was projected to average $25.7 trillion over the 2021–2030 period and to reach $30.7 trillion in 2030.) The differences between those two sets of projections illustrate that the rate of growth for federal spending on health programs has slowed significantly since 2010, but CBO has not analyzed how much of the difference between the projections is due to legislative changes, to updates to the agency's economic forecast, and to technical changes.

Question. While a portion of this difference relates to the repeal of the individual mandate and other policy changes, much of it appears to result from a sustained slowdown in health spending growth in recent years. In your January 2020 budget outlook, CBO noted that "The reasons for that slowdown are not clear." I think the slowdown prior to the COVID-19 pandemic is evidence that structural changes in the delivery of care – many of which were ushered in by the Affordable Care Act – have taken hold and we are seeing lower federal spending as a result. For example, Coastal Medical in Rhode Island, a Medicare Accountable Care Organization, has saved $25 million since 2015 and has done so while increasing services and improving the quality of care their patients receive. I think it's important for CBO to tease out what is responsible for this significant, sustained slowdown in federal health spending growth. What is CBO doing to better understand the causes of the sustained slowdown in federal health care spending?

16. See Congressional Budget Office, *The Long-Term Budget Outlook* (June 2010), www.cbo.gov/publication/21546.

Answer. CBO is monitoring the research literature and consulting with outside experts to increase its understanding of the causes of the slowdown in the growth of federal health care spending. For example, CBO invited Professor David Cutler of Harvard University to discuss that topic at the annual meeting of its Panel of Health Advisers in September 2019. Dr. Cutler pointed out that although a significant amount of research has been conducted to identify the causes of the slowdown in the growth of federal health care spending, a definitive conclusion has not been reached.

In CBO's estimation, the evidence points most clearly to two causes: decreases in the growth of Medicare payment rates and reduced spending on cardiovascular diseases due to better management of those conditions. CBO believes that the payment and delivery systems adopted by both public and private insurers that reward providers for delivering high quality care efficiently (rather than rewarding them for the number of services they provide) have also contributed to the slowdown in the growth of federal health care spending to some extent. However, it is challenging to estimate the magnitude of the effects of those payment and delivery systems because they may have led to systemwide changes in the practice of medicine that are difficult to attribute to any specific policies. CBO recognizes that understanding changes in health spending and the relationship between those changes and policy actions is an area of continuing Congressional interest. The agency is continuing to evaluate the research literature.

Medicare Payment Rates. Slower growth of Medicare payment rates has been a major factor contributing to the slowdown in the growth of Medicare spending in various ways. The ACA permanently reduced the annual payment updates in the Medicare fee-for-service (FFS) program for hospitals and other institutional providers by the projected growth in economy-wide productivity. (The ACA imposed additional reductions in the updates to payment rates through 2019 that varied by year and were, on average, smaller than the productivity-related reductions.) Those reductions in payment rate growth in the FFS program also slowed the growth of spending in the Medicare Advantage (MA) program, because benchmarks in the MA program are tied to per capita spending in the FFS program. The ACA also changed the method for establishing MA benchmarks, thereby reducing payments to MA plans. Additionally, the Budget Control Act of 2011 led to other across-the-board reductions in Medicare payments to providers through sequestration.

Those decreases in the growth of payment rates directly slowed the growth of Medicare spending by reducing the amount paid for each service. The slowdown in the growth of payment rates might have also contributed to a slowdown in the growth of the volume and complexity of services delivered. In a review of the literature CBO conducted to develop its capability to model the effects of implementing a single-payer health care system, the agency found that, on balance, the evidence indicates that providers respond to lower payment rates by reducing the quantity of services they provide.[17] The evidence is mixed, however, so CBO will investigate the issue more thoroughly in the coming year by continuing to monitor the research literature on how providers respond to changes in payment rates and by analyzing historical data on Medicare spending, payment rates, and utilization.

Spending on Cardiovascular Disease. A recent study suggests that greater use of medications to control risk factors for cardiovascular diseases may have played an important role in the

17. See CBO's Single-Payer Health Care Systems Team, *How CBO Analyzes the Costs of Proposals for Single-Payer Health Care Systems That are Based on Medicare's Fee-For-Service Program*, Working Paper 2020-08 (December 2020), www.cbo.gov/publication/56811.

slowdown in the growth of federal health care spending.[18] That study estimated that half of the slowdown in per capita spending among elderly Medicare beneficiaries from 1999 to 2012 was the result of slower growth in spending for cardiovascular diseases. The authors also estimated that half of the slowdown in hospitalizations for cardiovascular conditions was the result of greater use of medications to control risk factors such as hypertension, high cholesterol, and diabetes.

That study did not, however, investigate the reasons for the increased use of medications for cardiovascular disease among the elderly. One possible reason is that the implementation of the Medicare prescription drug benefit (Part D) in 2006 lowered out-of-pocket costs for prescription drugs for many seniors. In addition, some medications for cardiovascular diseases lost patent protection during the study period and less expensive generic versions became available. CBO has previously concluded that greater use of prescription drugs among Medicare beneficiaries reduces Medicare spending on medical services.[19] (That insight is incorporated in cost estimates such as that for the Elijah E. Cummings Lower Drug Costs Now Act, in which lower drug prices and out-of-pocket costs lead to increased use of drugs and thus less spending on other medical services).[20]

More research is needed to fully understand the reasons for the slowdown in the growth of spending on cardiovascular disease and to understand the relative roles of greater use of medications, lifestyle changes, and other factors. Additional research is also needed to understand the causes of changes in spending growth on other conditions. CBO will continue to monitor the research literature to improve its understanding of how the use of prescription drugs affects spending on medical services.

New Payment and Delivery Systems. The ACA instituted a variety of changes to payment and delivery systems including the Medicare Shared Savings Program for Accountable Care Organizations (ACOs) and other quality-based payment incentives. The ACA also established the Center for Medicare & Medicaid Innovation (CMMI) to test new payment models and delivery systems. Those changes built upon a decades-long shift in Medicare payment policy away from cost-based reimbursement to prospective payment. The changes instituted by the ACA also built upon earlier efforts by public and private insurers to adopt alternative payment and delivery approaches intended to reward providers for delivering care efficiently.

It is likely that those changes in payment and delivery methods led to structural changes in the health care system that contributed to the slowdown in the growth of federal health care spending, but the available evidence indicates that the changes in payment and delivery systems instituted by the ACA have not—by themselves—significantly reduced the growth of Medicare spending. For example, the most recent evidence indicates that ACOs have achieved only modest savings for Medicare after accounting for the shared savings bonuses they received.[21] CBO will continue to monitor the evidence on the effects of the payment and delivery systems in the ACA (including the models tested by CMMI) as well as evidence in the research literature on how other changes in payment and delivery systems implemented by public and private insurers have affected health care spending.

18. See David Cutler and others, "Explaining the Slowdown in Medical Spending Growth Among the Elderly, 1999–2012," *Health Affairs*, vol. 38, no. 2 (February 2019), pp. 222–229, https://tinyurl.com/y4nau678.

19. See Congressional Budget Office, *Offsetting Effects of Prescription Drug Use on Medicare's Spending for Medical Services* (November 2012), www.cbo.gov/publication/43741.

20. See Congressional Budget Office, cost estimate for H.R. 3, the Elijah E. Cummings Lower Drug Costs Now Act (December 10, 2019), www.cbo.gov/publication/55936.

21. See J. Michael McWilliams and others, "Medicare Spending After 3 Years of the Medicare Shared Savings Program," *New England Journal of Medicine*, vol. 392, no. 12 (September 20, 2018), pp. 1139–1149, https://doi.org/10.1056/NEJMsa1803388.

Question. Medicare Accountable Care Organizations like Coastal Medical in Rhode Island, have great flexibility to develop and implement innovative care models. In particular, ACOs are uniquely positioned to test preventive care models and demonstrate that coordinated care management and data collection can improve quality performance, including patient outcomes. Yet traditional fee-for-service Medicare is left behind when it comes to making similar investments because CBO's current "scoring" process discounts the savings of preventive health initiatives beyond the traditional 10-year scoring window. How can CBO modernize the way you score preventative health care?

Answer. Because Congressional budget enforcement procedures generally apply to a 10-year period, CBO estimates typically also have a 10-year window. However, the effects of some policies—health improvements and corresponding budgetary effects, for example—could occur outside the 10-year period. The occurrence of those budgetary effects and how they materialized over time would depend on the specific preventive medical service that was targeted. Potential long-term effects of proposed policies are certainly worth considering, even though they are not addressed by the current budget process. In some cases, such as a tax on tobacco products, CBO has analyzed the longer-term effects of a given policy.[22]

CBO analyzes legislative proposals on a case-by-case basis, considering the details of each proposal and drawing on relevant data and evidence. When estimating the effects of a proposal affecting preventive medical services, CBO has to assess factors such as the number of people who would use the preventive medical service in response to a policy, the average changes in health care spending and other outcomes, and the associated budgetary effects. In some cases, making those assessments is hindered by a lack of information, data, or empirical evidence, which in turn makes it difficult to estimate how a given intervention would affect federal spending.

There are some instances for which CBO has estimated that a policy to increase use of a preventive health service would be associated with a reduction in spending. One such example is a provision in the ACA that introduced coverage of tobacco cessation services for pregnant women under Medicaid. CBO estimated that the provision would reduce federal spending for that program by $100 million over the 2010–2019 period.[23] More recently, CBO analyzed a policy that would create a new Medicare benefit option that would cover the cost of immunosuppressive drugs for kidney transplant patients who had no other health insurance or drug coverage. On the one hand, use of immunosuppressive drugs could be considered part of treatment after a kidney transplant, but on the other hand, it could also be considered preventive care because those drugs prevent graft failure and subsequent need for dialysis treatments. CBO estimated that the creation of that new benefit would reduce spending for Medicare by $400 million over the 2021–2030 period.[24] In both cases, CBO estimated that the increase in federal costs associated with the policy would be outweighed by reductions in costs stemming from averted use of health care services.

Although increasing the use of preventive medical services may often improve people's health, it does not necessarily reduce federal spending. In most cases, reductions in federal spending

22. See Congressional Budget Office, *Raising the Excise Tax on Cigarettes: Effects on Health and the Federal Budget* (June 2012), www.cbo.gov/publication/43319.

23. See the Congressional Budget Office, letter to the Honorable Nancy Pelosi providing an estimate for H.R. 4872, the Reconciliation Act of 2010 (Final Health Care Legislation), Table 5 (March 20, 2010), www.cbo.gov/publication/21351.

24. See Congressional Budget Office, cost estimate for H.R. 5534, the Comprehensive Immunosuppressive Drug Coverage for Kidney Transplant Patients Act of 2020 (November 2, 2020), www.cbo.gov/publication/56726.

from averted use of health care services are smaller than the increase in federal costs of covering the preventive service for a broad set of patients. In June 2020, CBO released a report entitled *How CBO Analyzes Approaches to Improve Health Through Disease Prevention*, which provides a detailed description of the methods CBO has developed to estimate the budgetary effects of policies that affect preventive services.[25] That report also describes the results of a systematic review of the literature on the effects of preventive medical services and a detailed description of how CBO estimates the budgetary effects of policies that affect such services. Based on its review of the literature, which includes hundreds of studies, CBO concluded that many preventive services improve health, but only a small proportion of preventative services reduce costs. Specifically, the agency found that 20 percent of preventive medical services improve health and reduce costs; 60 percent provided clinical benefits that many people in the health care community considered to be reasonable relative to their costs, *but which did not reduce those costs*; and 20 percent either increased costs by an amount too large to justify their health benefits or worsened health.

Question. Over the last several months, there have been numerous new reports out detailing the serious economic risks of climate change.

- In January, the Bank of International Settlements, the central bank for central banks, issued a report on climate-related economic risk in which it stated, "[C]limate change is a source of major systemic financial risks;" "[C]limate catastrophes are even more serious than most systemic financial crises;" and "Exceeding climate tipping points could lead to catastrophic and irreversible impacts that would make quantifying financial damages impossible."

- In January, McKinsey issued a report on climate-related economic risk in which it stated, "Intensifying climate hazards could put millions of lives at risk, as well as trillions of dollars of economic activity and physical capital, and the world's stock of natural capital.

- In January, the Stanford Graduate School of Business released a report in which it stated, "global economic losses from climate change could reach $23 trillion—three or four times the scale of the 2008 financial crisis."

- In September, the Commodity Futures Trading Commission released a report on climate-related economic risks in which it stated, "Climate change poses a major risk to the stability of the U.S. financial system and to its ability to sustain the American economy. Climate change is already impacting or is anticipated to impact nearly every facet of the economy, including infrastructure, agriculture, residential and commercial property, as well as human health and labor productivity. Over time, if significant action is not taken to check rising global average temperatures, climate change impacts could impair the productive capacity of the economy and undermine its ability to generate employment, income, and opportunity."

In light of the severe potential financial and economic costs of climate change, does it make economic sense to roll back regulations limiting greenhouse gas emissions?

Answer. CBO has assessed the economic and budgetary impacts of various policies intended to reduce greenhouse gas emissions. For instance, the agency has analyzed the potential

25. See Congressional Budget Office, *How CBO Analyzes Approaches to Improve Health Through Disease Prevention* (June 2020), www.cbo.gov/publication/56345.

impacts of carbon taxes, cap-and-trade programs, funding for research and development, and regulatory approaches such as a clean electricity standard.[26] However, CBO has not conducted a cost-benefit analysis of any specific regulations intended to limit greenhouse gas emissions. Both costs and benefits would depend on specifics of the regulation (including its stringency and the extent to which it would motivate emission reductions in a cost-effective manner) and on the actions taken by other countries.

Policymakers' choices about climate change will involve tradeoffs between the climatic effects of greenhouse gas emissions (on GDP and aspects of people's future well-being not captured in GDP) and the cost of ameliorating those effects through regulations or other actions. CBO projects that the continued emission of greenhouse gases will, on net, reduce average annual real GDP growth from 2020 to 2050 relative to growth under the climatic conditions that prevailed at the end of the 20th century.[27] That annual growth differential will accumulate to a 1.0 percent reduction in the projected level of real GDP in 2050, CBO estimates.

That estimate is a central projection, which means that it represents the middle of a wide range of potential outcomes. Consistent with the best available research, CBO's approach allows for both positive and negative effects of climate change; however, it does not incorporate every possible effect of climate change on GDP and is subject to substantial uncertainty. The uncertainty around those estimates and the potential for substantial damage increase over time. In addition, climate change may affect people's well-being in ways that are not measured in GDP, such as premature mortality changes.

Question. The number of climate-related natural disasters continues to grow. In just the last two months, we've seen Hurricanes Laura and Sally devastate parts of the Gulf Coast while unprecedented wildfires have burned through communities in California and the Pacific Northwest. Do you believe it is economically sustainable to have to spend tens or hundreds of billions of dollars per year on disaster relief?

Answer. When disasters occur, lawmakers face choices about whether to provide disaster assistance and how much to spend. Increased frequency and severity of disasters are expected to increase calls for disaster spending in the future. In particular, damage from hurricanes is expected to increase significantly in the coming decades because of the effects of both climate change and increased coastal development. In turn, requests for federal relief and recovery efforts may potentially increase as well.

In 2016, CBO estimated that, over time, the costs associated with hurricane damage will increase more rapidly than the economy will grow.[28] Consequently, hurricane damage will rise as a share of GDP, which provides a measure of the nation's ability to pay for that

26. See, for example, Congressional Budget Office, *Options for Reducing the Deficit: 2019 to 2028* (December 2018), pp. 292–294, www.cbo.gov/publication/54667; *Federal Support for the Development, Production, and Use of Fuels and Energy Technologies* (November 2015), www.cbo.gov/publication/50980; *Effects of a Carbon Tax on the Economy and the Environment* (May 2013), www.cbo.gov/publication/44223; *Effects of Federal Tax Credits for the Purchase of Electric Vehicles* (September 2012), www.cbo.gov/publication/43576; *The Effects of Renewable or Clean Electricity Standards* (July 2011), www.cbo.gov/publication/41451; and cost estimate for H.R. 2454, American Clean Energy and Security Act (June 5, 2009), www.cbo.gov/publication/41189.

27. See Evan Herrnstadt and Terry Dinan, *CBO's Projection of the Effect of Climate Change on U.S. Economic Output*, Working Paper 2020-06 (Congressional Budget Office, September 2020), www.cbo.gov/publication/56505.

28. See Congressional Budget Office, *Potential Increases in Hurricane Damage in the United States: Implications for the Federal Budget* (June 2016), www.cbo.gov/publication/51518.

damage. According to the agency's estimates, expected annual damage currently amounts to 0.16 percent of GDP; by 2075, that figure reaches 0.22 percent. (Changes in expected damage reflect the increase in the probability of a major hurricane making landfall in the United States and that if one did make landfall, damage would probably be greater as a result of higher sea levels and increased coastal development; actual damage will vary substantially from year to year.) Roughly 45 percent of that increase is attributable to climate change and 55 percent to coastal development. The uncertainty associated with those estimates is substantial and increases over time.

CBO estimated annual federal spending for relief and recovery as a percentage of expected hurricane damage. If that percentage stays roughly the same as it was from 2005 to 2015 (the period used as the basis of CBO's 2016 federal spending estimates), relief and recovery spending would rise from 0.10 percent of GDP under current conditions to 0.13 percent of GDP in 2075. Such an increase would be equivalent to about $6 billion, measured as a share of GDP in 2020. If federal spending as a percentage of hurricane damage changed, those amounts could be larger or smaller.

Resources devoted to disaster relief and recovery could otherwise be used productively elsewhere in the economy. As a result, an increase in hurricane damage to buildings, infrastructure, or other capital could dampen future economic growth in the United States.[29]

Question. In CBO's report on the Effects of Pandemic-Related Legislation, you project that the related bills passed by Congress in 2020 would increase GDP by 3.1% in 2021. What else should Congress be doing now to support economic recovery in 2021 and beyond?

Answer. CBO can analyze alternative policy proposals and their effects on the economy, but in keeping with its mandate to provide objective and impartial analysis, the agency does not make policy recommendations.

Question. Small businesses are particularly important to Rhode Island's economy, and over the last several months, I have heard from many businesses about their struggles throughout the pandemic and the uncertainty about their future. The PPP program ended on August 8, without additional assistance many small businesses will continue to struggle and could potentially close in the months ahead.

- If Congress fails to provide our nation's small businesses with additional assistance to get them through the rest of the year or longer, how would that affect the economy in 2021 and beyond? How would that affect the unemployment rate?

- Do you agree that providing small businesses with more assistance now would help stave off even more economic pain later?

Answer. The effects of more assistance to small businesses would depend on the design and implementation of those policies. CBO analyzed how support provided by recent legislation affected small businesses in its report entitled *The Effect of Pandemic-Related Legislation on Output* and a related paper entitled *Key Methods That CBO Used to Estimate the Effects of*

29. See Evan Herrnstadt and Terry Dinan, *CBO's Projection of the Effect of Climate Change on U.S. Economic Output*, Working Paper 2020-06 (Congressional Budget Office, September 2020), p. 2, www.cbo.gov/publication/56505; and Congressional Budget Office, *Potential Increases in Hurricane Damage in the United States: Implications for the Federal Budget* (June 2016), www.cbo.gov/publication/51518.

Pandemic-Related Legislation on Output.[30] In those analyses, CBO estimated that for every dollar of budgetary cost, the PPP and related provisions increased GDP by 36 cents from fiscal year 2020 through 2023 (the majority of which is projected to occur in the second half of 2020). The PPP was projected to save 106 million job-weeks in 2020 (a job-week is one week of work for an average worker whose job had been lost due to the pandemic).

Additional assistance for small businesses would boost the economy and reduce unemployment in 2021. The magnitude of those effects would depend on the form and amount of the assistance. However, a deficit-financed fiscal stimulus would also decrease output in the long term in several ways: It would add to the already growing stock of debt, increase interest rates, and crowd out private investment. Those long-term effects would be modest over the next few years because interest rates are expected to remain low as a result of actions taken by the Federal Reserve.

Question. Many state and local governments have faced financial difficulties as a result of the costs of the pandemic and decreases in tax revenue. Without further assistance to state and local governments to help offset the fiscal issues caused by the pandemic we risk additional job losses in our communities and the elimination of essential services. If state and local governments do not receive additional relief and are forced to take drastic measures to make up for budget shortfalls caused by the pandemic, how would that affect the national economy next year?

Answer. The pandemic and the associated social distancing measures have significantly affected the finances of state and local governments by reducing current and projected tax revenues and creating additional spending demands. CBO estimates that the direct assistance already provided by pandemic-related legislation will be disbursed to state and local governments during calendar year 2020; most of that assistance was provided for specific purposes and will amount to less than the governments lose in tax revenues this year. In the 2007–2009 recession and subsequent recovery, state and local governments experienced similar fiscal pressure. They responded mainly by reducing spending on education, health, and social services. Some of those reductions were achieved by cutting public-sector employment.[31]

State and local government employment declined by 13,000 in November and was 1.3 million (or 6.8 percent) below its February level. If state and local government layoffs persist or if job growth is muted, state and local government purchases of goods and services—which accounted for roughly 11 percent of GDP in 2019 and is primarily the compensation paid by those governments to their employees—would not quickly recover to its pre-pandemic level.[32] A decline or slow growth in real (inflation-adjusted) state and local government purchases would slow the economic recovery.

30. See Congressional Budget Office, *The Effect of Pandemic-Related Legislation on Output* (September 2020), www.cbo.gov/publication/56537; and John Seliski and others, *Key Methods That CBO Used to Estimate the Effects of Pandemic-Related Legislation on Output*, Working Paper 2020-07 (Congressional Budget Office, October 2020), www.cbo.gov/publication/56612.

31. For details, see Tracy Gordon, "State and Local Budgets and the Great Recession" (December 31, 2012), https://tinyurl.com/y4aqzcvj.

32. In the national income and product accounts, the Bureau of Economic Analysis (BEA) reports government spending in three ways: government purchases (which BEA officially refers to as government consumption expenditures and gross investment), government current expenditures, and total government expenditures. For more information, see Bureau of Economic Analysis, "BEA Seems to Have Several Different Measures of Government Spending. What are They for and What do They Measure?" (May 28, 2010), www.bea.gov/help/faq/552. State and local governments' purchases have been about three-quarters as large as their total spending over the past few years. State and local governments' total spending includes some items, such as Medicaid expenditures, that are not included in state and local governments' purchases but are instead transfers to people.